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EX PARTE OR LATE FILED



28 February 1994

Mr. Bruce Franca
Mr. Alan Stilwell
C/O Secretary
FCC
1919 M St, NW
Rm 222
Washington, DC 20554



RE: ET Docket No. 93-7
Compatibility Between Cable Systems and
Consumer Electronics Equipment

EX PARTE

Dear Bruce and Alan:

I am writing to express my deep concern that you may not allow a separate equipment charge for back-of-set descramblers. Both Wendell Bailey and Bob Unger suggested that I contact you to clarify certain issues which they discussed with you during a recent meeting. Following are brief discussions of the issues Wendell and Bob mentioned.

The 11.25% return on invested capital is not appealing.

Corporations raise capital by issuing stock (equity) and by borrowing. Highly leveraged firms which can no longer borrow at reasonable rates are forced to sell stock to raise capital. An example is Aldelphia's recent issue of equity securities. Because a firm's capitalization consists of both equity and debt, the proper cost of capital is computed as a market value weighted average of both elements. Equity rates are substantially (6%+) higher than debt rates for most firms and the weighted average cost of capital is usually higher than the borrowing rate.

A recent issue of *Fortune* listed the cost of capital for leading US firms, including Coca-Cola, Procter & Gamble, McDonald's and many others. The computed average cost of capital for the top 100 firms was 11.5%.

As highly leveraged cable firms with uncertain future cash flows are forced to equity markets, investors will want returns far in excess of 11.25%. Thus, the notion that cable firms can consistently raise capital at rates below 11.25% is false.

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List ABCDE

A handwritten signature in cursive script, appearing to be "Quigley", written over the "List ABCDE" text.

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Even if you ignore the realities of capital markets, the Commission staff has recommended 11.25% as the appropriate capital cost recovery rate for boxes.

Even if 11.25% were appealing, capital will be scarce.

If capital were abundant, operators would still be indifferent to an investment which only covered their cost of capital. (\$0 value added). However, capital will be scarce for cable companies in the wake of the February 22 rate reduction which will severely decrease free cash flows. For example, TeleCable placed its largest fiber and coaxial upgrade projects on permanent hold on February 23rd. Many other operators have announced similar plans. The result of reduced and uncertain cash flows will be that only the most attractive or essential projects will be funded (returns well in excess of 11.25%). Therefore, worries that cable operators will go on decoder spending sprees because they are incented by an 11.25% return, are unfounded.

An equipment charge for a back-of-set descrambler is fair.

The cost for a back-of-set descrambler which gives the consumer the same functionality as today's set-top descrambler will be less. Based upon estimates given by two leading suppliers, analog back-of-set descramblers will cost \$40 less than their analog set-top counterparts. Total monthly savings are estimated to be \$0.81 which will pay back the \$18 (Thompson CE estimate) investment in the decoder interface within 22 months. With a reduced equipment charge, those persons who elect to purchase TVs and VCRs with decoder interface connectors will benefit. Those who do not elect to purchase new TVs and VCRs will not inadvertently subsidize those who do.

Back-of-set descramblers will benefit consumers and program suppliers as well as cable operators.

Wendell told me of your argument that the component descramblers and therefore scrambling exists solely for the benefit of the cable operator. In fact, scrambling is the only feasible means of securing multiple signals in a cable system. That will be even more true in the future. Just as a security system in a retail store benefits consumers and suppliers of merchandise in addition to store owners, scrambling systems benefit cable customers who are willing to pay for services and assures a continued supply of programming from content creators.

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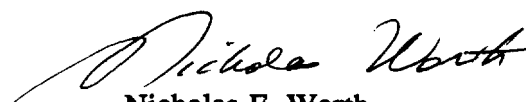
If cable operators are prohibited from recovering costs for back-of-set decoders, they will lack the incentive necessary to make the decoder interface solution work.

The success of the decoder interface will depend upon the voluntary, creative efforts of many in the cable industry and much voluntary work remains to be done. Punishing cable operators by preventing them from recovering costs for back-of-set decoders will strongly discourage any further voluntary efforts. Who would volunteer to build his own gallows?

I hope that this information is helpful to you. Without a fair ruling, I fear that many hours of fine effort by individuals in the consumer and cable industries will go down the drain.

Very truly yours,

TELECABLE CORPORATION



Nicholas E. Worth

Executive Vice President

Engineering

NEW/krw

cc: Wendell Bailey, NCTA
Jim Colthorpe, FCC
Paul Glist, Cole, Raywid & Braverman
Bill Johnson, FCC
Maureen O'Connel, FCC
Merrill Spiegel, FCC
Tom Stanley, FCC
Sandy Wilson, FCC